

Office of Chief Counsel
Internal Revenue Service

memorandum

CC:NER: [REDACTED]: TL-N-3699-99
[REDACTED]

date:

to: Manager, Group 1710
ATTN: [REDACTED]

from: [REDACTED]
Associate District Counsel, [REDACTED] District, [REDACTED]

subject: [REDACTED]-Request for Advice on Consolidated Return
UIL Nos. 1501.00-00; 1504.02-00

DISCLOSURE STATEMENT

This advice constitutes return information subject to I.R.C. § 6103. This advice contains confidential information subject to attorney-client and deliberative process privileges and if prepared in contemplation of litigation, subject to the attorney work product privilege. Accordingly, the Examination or Appeals recipient of this document may provide it only to those persons whose official tax administration duties with respect to this case require such disclosure. In no event may this document be provided to Examination, Appeals, or other persons beyond those specifically indicated in this statement. This advice may not be disclosed to taxpayers or their representatives.

This advice is not binding on Examination or Appeals and is not a final case determination. Such advice is advisory and does not resolve Service position on an issue or provide the basis for closing a case. The determination of the Service in the case is to be made through the exercise of the independent judgment of the office with jurisdiction over the case.

This responds to your request for advice in the captioned matter. This advice is being reviewed by the National Office under 10-day post-review procedures and is subject to change.

ISSUE

May a corporation file consolidated returns with corporations formed under [REDACTED] law as non-stock, non-profit corporations to practice medicine?

CONCLUSION

Yes. The issuance of stock is not a prerequisite to filing consolidated returns on the facts presented here. Further, the role of the parent corporation in the medical practices does not violate corporate practice of medicine doctrine.

FACTS

an I.R.C. § 501(c)(3) organization, owns all of the stock of a for-profit corporation. began acquiring medical practices in this decade and has acquired over practices to date.

According to , as of , it was the sole member (a term explained in greater detail below) of over medical practices, each of which was organized as a nonstock/nonprofit corporation under law. is also members of other medical practice corporations. also owns all of the stock of , a corporation which provides management services to all of the other corporations owned by .

For years ending prior to June 30, , and the medical practices filed separate returns. For the years ending June 30, , and June 30, , filed consolidated returns with and the medical practice corporations of which it was the sole member (the medical practice corporations of which it was members were not part of the consolidated filings). Many of the medical practices experienced losses for , and the consolidated filing enabled to claim a \$ net operating loss.

You have inquired whether may file consolidated returns with the medical practices in light of their nonstock/nonprofit status and in light of corporate practice of medicine doctrine.

DISCUSSION

law permits the formation of corporations as nonstock corporations. , et seq. As their name implies, nonstock corporations do not issue shares of stock. Instead, the corporations have members. Each member

of record of a nonstock corporation has the right to one vote at every meeting of members, except as provided in the corporation's bylaws or in a written document evidencing membership. [REDACTED]

According to the taxpayer [REDACTED] is the sole member of all but [REDACTED] of the medical practices and is [REDACTED] members of those [REDACTED] practices. As the sole member of the medical practice corporations, [REDACTED] would be entitled to surplus assets on dissolution of any of the corporations. [REDACTED]

[REDACTED] law also permits the formation of nonprofit corporations.

Under I.R.C. § 1501, an affiliated group of corporations is granted the privilege of filing a consolidated income tax return. Generally speaking under I.R.C. § 1504, an affiliated group of corporations is one in which:

- a) The corporations are connected through stock ownership with a common parent corporation;
- b) Each corporation is an includible corporation within the meaning of I.R.C. § 1504(b); and
- c) The includible corporations are connected through stock ownership with a common parent corporation, which is an includible corporation, if:
 - (i) the parent directly owns at least 80 percent of the voting power of all outstanding stock and at least 80 percent of the value of the outstanding stock of at least one other includible corporation; and
 - (ii) at least 80 percent of the voting power and 80 percent of the value of all outstanding stock of each corporation (except the common parent) is owned directly by one or more of the other includible corporations.

One obvious issue is whether a group of corporations which do not issue stock may be part of an affiliated group of corporations in light of the stock ownership requirements of I.R.C. § 1504.

In Letter Ruling 8913209, the IRS responded to a taxpayer's request for a ruling that its membership interest in a subsidiary organized on a nonstock basis under state law be treated as stock ownership, thereby enabling the subsidiary to be an

includible member of the parent's affiliated group under I.R.C. § 1504. The requesting taxpayer was the sole member of the nonstock subsidiary. The IRS concluded in the ruling that the requesting taxpayer's membership interest in the subsidiary was to be treated as stock ownership and that, provided that the parent's membership interest in the subsidiary possessed at least 80% of the vote and value of the subsidiary, and further provided that the parent made basis adjustments under Treas. Reg. § 1.1502-32 in its membership interest in the subsidiary as if such membership interest were shares of stock of the subsidiary, the subsidiary was a member of the parent's affiliated group and could join in the filing of a consolidated federal income tax return with the parent.

The ruling relies in part on Rev. Rul. 69-591, 1969-2 C.B. 172. That ruling holds that an affiliated group may come into existence, notwithstanding the absence of actual stockholding in a subsidiary. Rev. Rul. 69-591 provides that the term "stock" as used in the consolidated return provisions is not restricted to cases where formal certificates have been issued, but is considered as having the meaning of "shares of stock," i.e., the right which the owner or owners have in the management, profits and ultimate assets of corporation.

We conclude, subject to the same provisos as were stated in Letter Ruling 8913209 regarding voting power and value (which we have no reason to question in this case), and further subject to Treas. Reg. § 1.1502-32 basis adjustments (which you should verify), that [REDACTED] may include the medical practice corporations of which it is the sole member in its consolidated return filing.

The corporate practice of medicine doctrine as it exists in [REDACTED] does not alter our conclusion. In [REDACTED] the Supreme Court of [REDACTED] stated the general rule that a licensed practitioner of a profession may not lawfully practice his profession as an employee of a corporation and if he does so, the corporation employing him may be guilty of practicing the profession without a license. The reason for the rule is that the employee will owe his first loyalty to his employer and will have less incentive to maintain high professional standards and obey regulations governing the profession if he has no contractual relationship with the patient and merely practices as the employee of an entity whose primary objective is profit. [REDACTED]

The corporate practice of medicine doctrine has been pared down by statute. Thus, for example, professional corporations ([REDACTED]), health maintenance

organizations ([REDACTED]) and professional health plan corporations ([REDACTED], et seq.) may employ physicians. Prior to February, 1998, regulations promulgated by the [REDACTED] Department of State provided that a nonprofit corporation could not provide professional services. [REDACTED]. In [REDACTED], [REDACTED], the Department determined that the regulation was overbroad and contrary to statute. It repealed [REDACTED]. Thus, there is now no bar to the provision of medical services and, therefore, the employment of physicians by nonprofit corporations in [REDACTED].

Based on the foregoing, we conclude (subject to previously stated provisos) that [REDACTED] may include the nonstock/nonprofit medical practices in which it is the sole member in its consolidated income tax return for [REDACTED] and [REDACTED].

Please call [REDACTED] at ([REDACTED]) [REDACTED] if you have any questions.

[REDACTED]
Associate District Counsel